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RESEARCH ARTICLE

Business-Government Networks in Small States: The Emergence and Evolution of the Luxembourg Global Mutual Fund Industry, 1945–1988

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Abstract

This research reconstructs the business dynamics behind the evolution of the European mutual fund industry, which led Luxembourg to become its main international gateway since the 1960s. We analyze this local industry to understand how political and financial elites influence the economic specialization of small states. We argue that a closely-knit community of local professionals and politicians, well-versed in corporate and European legislation, leveraged the Grand Duchy's small state status within the nascent European Community to become a financial hub specializing in mutual funds within an emerging network of international financial centers. This position was achieved through bifurcation of sovereignty strategies on the basis of two main premises. First, on the systematic acceptance of conflicts of interest within local financial and political leadership, comprising overlapping roles, revolving-doors, and familial ties in business relationships. Second, on regulatory engineering practices, such as the dynamic interpretation of laws, and the strategic planning of directive assimilation to advance Luxembourg's interests as opposed to its EU counterparts. The analysis uses archival material from nine archival collections and oral history interviews.

Keywords: mutual funds; Luxembourg; small states; communities of experts; tax avoidance

By the early 2020s, the aggregate net assets of mutual funds worldwide amounted to around USD 70 trillion, with the United States and Luxembourg as the first and second largest issuers, respectively. By this time, Luxembourg led the European market of mutual funds with aggregate assets of more than USD 6 trillion.[1]

[1] "Politique d'investissement des OPC. Situation au 29 février 2024," Commission de Surveillance du Secteur Financier (CSSF), accessed 29 March 2024, www.cssf.lu/fr/2023/01/politique-dinvestissement-des-opc/. Mutual funds are open-ended investment vehicles that pool capital from multiple

Between the end of World War II (WWII) and the end of the 1980s, the small state of Luxembourg transformed from a peripheral center whose economy was originally based on the production and export of agricultural goods and steel into a global financial cluster specializing in domiciliation and trading of mutual funds.[2] From these premises, we used the Luxembourg mutual fund industry as a case to understand how business elites and their relationships with politics influence the economic specialization of small states.

Incorporations of investment trusts, prototypes of modern investment funds, can be traced back to the interwar years in continental Europe. The emergence of these early investment funds can be connected to the reaction of the international business environment to changes in corporate regulation following World War I (WWI), typically in countries introducing progressive taxation.[3] During WWI, the Allied naval blockade of Germany had thwarted strategies to dodge sanctions, such as diverting commercial flows to neighboring neutral states like Sweden, trading through shell companies to conceal ownership, and using Swiss and Dutch banks to channel capital.[4] Several of these practices were repurposed and refined in the interwar period to

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investors to construct and manage a diversified portfolio of financial assets. They operate with a variable capital structure, continuously issuing and redeeming shares at net asset value (NAV). Unlike closed-end funds, which trade on secondary markets, mutual funds provide direct liquidity to investors through NAV-based redemptions. Portfolio composition is actively or passively managed by a professional management firm, subject to regulatory oversight. See Janette Rutterford, "Learning from One Another's Mistakes: Investment Trusts in the UK and the US, 1868–1940," *Financial History Review* 16, no. 2 (2009): 157–181; Dimitris P. Sotiropoulos, Janette Rutterford, and Carry van Lieshout, "The Rise of Professional Asset Management: The UK Investment Trust Network Before World War I," *Business History* 63, no. 5 (2021): 826–849; John Morley, "The Separation of Funds and Managers: A Theory of Investment Fund Structure and Regulation," *The Yale Law Journal* 123, no. 5 (2014): 1228–1287; K. Geert Rouwenhorst, "The Origins of Mutual Funds," in *The Origins of Value, the Financial Innovations that Created Modern Capital Markets*, ed. Will N. Goetzmann and K. Geert Rouwenhorst (Oxford, 2005), 249–269.

[2] Gilbert Trausch, *Histoire Economique Du Grand-Duché de Luxembourg*, 1815–2015 (Luxembourg, 2017); Sabine Dörry, "Strategic Nodes in Investment Fund Global Production Networks: The Example of the Financial Centre Luxembourg" *Journal of Economic Geography* 15, no. 4 (2015): 797–814.

[3] Matteo Calabrese and Benoît Majerus, "Archaeology of a Treasure Island. Actors and Practices of Holding in Luxembourg (1929–1940)," *Contemporary European History* 33, No. 4 (2024): 1398-1415; Christophe Farquet, *La défense du paradis fiscal Suisse avant la Seconde Guerre mondiale: Une histoire internationale* (Neuchâtel, 2016); Christophe Farquet, "Le marché de l'évasion fiscale dans l'entre-deux-guerres," *L'Économie politique* 2, no. 54 (2012): 95–112.

[4] John McDermott, "Trading with the Enemy: British Business and the Law during the First World War," *Canadian Journal of History* 32, no. 2 (1997): 201–219; James Hollis and Christopher McKenna, "The Emergence of the Offshore Economy, 1914–1939," in *Capitalism's hidden worlds*, ed. Kenneth Lipartito and Lisa Jacobson (Philadelphia, 2020), 157–177; Cees Wiebes and GH Aalders, *The Art of Cloaking Ownership. The Case of Sweden. The Secret Collaboration and Protection of the German War Industry by the Neutrals* (Amsterdam, 1996); Geoffrey Jones and Christina Lubinski, "Managing Political Risk in Global Business: Beiersdorf 1914–1990," *Enterprise and Society* 13, no. 1 (2012): 85–119; Christopher Kobrak and Jana Wüstenhagen, "International Investment and Nazi Politics: The Cloaking of German Assets Abroad, 1936–1945," *Business History* 48, no. 3 (2006): 399–427; Marc Frey, "Trade, Ships, and the Neutrality of the Netherlands in the First World War," *The International History Review* 19, no. 3 (1997): 541–562.

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eschew increased taxes, surging barriers to trade, and capital flows, shaping the new deglobalizing world economy.[5]

The need for multinationals and wealthy families to divert capital away from home countries represented a significant growth opportunity, especially for small-sized, neutral, and multilingual countries, such as Switzerland, and Luxembourg.[6] As argued by Calabrese and Majerus, in this early phase, Luxembourg already implemented capital encoding practices that utilized the specialized legal and financial knowledge of the local community of legal professionals.[7] Furthermore, the country's small size facilitated initiatives across different spheres of influence, including political, financial, and legal, enabling these individuals to effectively collaborate and leverage their expertise in managing financial services and tax avoidance strategies.[8]

So far, the historical work on the development of offshore finance and tax avoidance in the context of small states remains limited to seminal works, such as historian Vanessa Ogle's and economist Gabriel Zucman's.[9] The historical scholarship on small states engaged in offshoring has concentrated on analyses of individual countries' developmental paths, most typically in contrast with "large" ones.[10] As for tax avoidance, business history has treated it in connection with the study of financialization and the development of international finance, and focused on how it affected corporate strategies and organizational choices.[11] However, this literature has not sufficiently analyzed the network mechanisms underlying the emergence of

[5] Farquet, "Le marché"; Geoffrey Jones, *Multinationals and Global Capitalism* (Oxford, UK, 2005); Daniela L. Caglioti, "Property Rights in Time of War: Sequestration and Liquidation of Enemy Aliens' Assets in Western Europe during the First World War," *Journal of Modern European History* 12, no. 4 (2014): 523–545.

[6] Serge Paquier, "Swiss Holding Companies from the Mid-Nineteenth Century to the Early 1930s: The Forerunners and Subsequent Waves of Creations," *Financial History Review* 8, no. 2 (2001): 163–182; Sébastien Guex, "The Emergence of the Swiss Tax Haven, 1816–1914," *Business History Review* 96 (2022): 353–372; Pierre Eichenberger, "Swiss Capitalism, or the Significance of Small Things," *Capitalism: A Journal of History and Economics* 3 (2022): 215–252; Farquet, *La défense du paradis fiscal Suisse*.

[7] Calabrese and Majerus, "Archaeology"; Benoît Majerus, "From Local Notables to Global Players: Law Firms in a Tax Haven (Luxembourg, 1960s to 2020s)," *Business History* (advance online publication, 13 Dec. 2024), accessed 5 March 2025, https://doi.org/10.1080/00076791.2024.2428956; Katharina Pistor, *The Code of Capital: How the Law Creates Wealth and Inequality* (Princeton, NJ, 2019); Benoît Majerus, "This Is Not a Scandal in Luxembourg," *Entreprises et histoire* 101, no. 4 (2020): 75–87 here: 75.

[8] Calabrese and Majerus, "Archaeology."

[9] Vanessa Ogle, "Archipelago Capitalism: Tax Havens, Offshore Money, and the State, 1950s–1970s," *American Historical Review* 112, no. 5 (2017): 1431–158; Gabriel Zucman, *The Hidden Wealth of Nations: The Scourge of Tax Havens* (Chicago, 2015); William Vlcek, *Offshore Finance and Small States: Sovereignty, Size and Money* (New York, 2008).

[10] Guex, "Swiss Tax Haven"; Sébastien Guex and Hadrien Buclin, *Tax Evasion and Tax Havens Since the Nineteenth Century* (Berlin, 2023); Eichenberger, "Swiss Capitalism."

[11] Youssef Cassis, *Capitals of Capital: The Rise and Fall of International Financial Centres, 1780–2009* (New York, 2010); Carlo E. Altamura, "A New Dawn for European Banking: The Euromarket, the Oil Crisis and the Rise of International Banking," *Zeitschrift für Unternehmensgeschichte* 60, no. 1 (2015): 29–51.Ryo Izawa, "Corporate Structural Change for Tax Avoidance: British Multinational Enterprises and International Double Taxation Between the First and Second World Wars," *Business History* 64, no. 4 (2022): 704–726; Simon Mollan, Billy Frank, and Kevin Tennent, "Changing Corporate Domicile: The Case of the Rhodesian Selection Trust Companies," in *International Business, Multi-Nationals, and the Nationality of the Company*, ed. Gehlen, Boris, Christian Marx, and Alfred Reckendrees, eds. (New York, 2023), 65–87.

financial infrastructure and small states' specialization in financial services and tax avoidance activities.

In this paper, we examine the process behind Luxembourg's financial specialization in mutual funds and its historical trajectory toward becoming a node in the global network of tax avoidance through this financial product.[12] In so doing, we aim to understand how the connections between business and government impacted the process of financial specialization in the context of a small country: how did business elites involved in the Luxembourg fund industry influence the country's policymaking and subsequent specialization in this financial service?

In Luxembourg, elements typical of a small state's socioeconomic and political context, such as a dense community of professionals and experts, and a corporatist tradition, contributed to crafting and continuously applying specific strategies, including several forms of conflict of interest and regulatory engineering. We define "conflict of interest" as the systematic acceptance of overlapping roles and revolving-door practices among the local financial and political elites. With "regulatory engineering," we refer to the development of juridical frameworks to better enact specific regulations that provide a competitive advantage in attracting capital, such as the dynamic interpretation of laws and the strategic planning of European directives assimilation.[13] These strategies allowed Luxembourg to achieve and preserve its advantage as a mutual fund and tax avoidance hub by leveraging its status as a founding partner of the European Community and its small size compared with other European counterparts, thus using the "power of being powerless" inherent to small states.

This research draws from diverse archival sources from physical collections and online repositories. Additionally, we integrated three in-depth oral histories conducted between 2021 and 2023 with influential personalities operating within Luxembourg's mutual fund industry since the 1970s. The next section introduces the theoretical framework and discusses the multidisciplinary literature on small states and communities of experts; the following section presents the data and methods we used for this research. Three empirical sections follow, presenting a historical analysis of how Luxembourg's business and government elites contributed to the emergence, expansion, and strengthening of the local mutual fund industry within the European context, which in turn helped the Grand Duchy become a major financial and tax avoidance hub. The last section concludes and discusses avenues for future research.

Communities of Experts in Small States

The scholarship on the development of the Luxembourg financial industry has shown that the local Luxembourgish elites played a crucial role in shaping the country's path toward becoming an international financial center.[14] Throughout the twentieth century, Luxembourg's governing class expanded to include a growing network of highly educated individuals operating at the intersection of the political and financial

[12] Zucman, *The Hidden Wealth of Nations*.

[13] Pistor, *The Code of Capital*; Majerus, "This Is Not a Scandal," 75.

[14] Sabine Dörry, "The Role of Élites in the Co-Evolution of International Financial Markets and Financial Centres: The Case of Luxembourg," *Competition & Change* 20, no. 21–36 (2016); Samuel Weeks, "Channeling the Capital of Others: How Luxembourg Came to Be Asset Managers' 'Plumber' of Choice," *Environment and Planning A: Economy and Space* 56, no. 2 (2024): 627–644.

milieus.[15] These were hybrid figures, holding both political mandates (i.e., in the Parliament) and professional roles (for instance, on the boards of banks, holding companies and financial surveillance bodies), who proved able to conjugate the embeddedness and informality of small circles where "everybody knows everybody" with a constant process of increasing exposure towards cosmopolitan entrepreneurs and wealthy families.[16] The development and exchange of specialized knowledge in finance and the overlapping roles of these communities of professionals operating across business and political spheres allowed them to foresee new trends in demand for financial services and adapt to changing circumstances in the Grand Duchy's economy.[17]

Through the Luxembourg case, we aim to connect the multidisciplinary literature on small states with the business history literature on business-government relationships, focusing on the strategies and organizational solutions implemented to foster specialization in mutual funds. Interdisciplinary literature on the size of states supports the idea that smaller countries benefit from greater agility in decision-making and policy implementation, often allowing for rapid adaptation to global changes.[18] The concept of a "small state" is debated, and typically defined using three criteria: a population under 1.5 million, limited usable land area, and a constrained gross national product.[19] Across disciplines like international relations,[20] political economy,[21] and development studies,[22] small states are viewed, and view themselves as vulnerable,[23] with limited military power and economic resources,[24] making them susceptible to external shocks,[25] and heavily

[15] Calabrese and Majerus, "Archaeology."

[16] Marlene Jugl, *Country Size and Public Administration* (Cambridge, UK, 2022), 68; Majerus, "Local Notables."

[17] Dörry, "The Role of Élites."

[18] Godfrey Baldacchino and Anders Wivel, "Small States: Concepts and Theories," in *Handbook on the Politics of Small States*, ed. Godfrey Baldacchino and Anders Wivel (Cheltenham, UK, 2020), 2–19; Robert Steinmetz and Anders Wivel, *Small States in Europe: Challenges and Opportunities* (London/New York, 2016).

[19] Tom Crowards, "Defining the Category of 'Small' States," *Journal of International Development* 14, no. 2 (2002): 143–179; Matthias Maass, "The Elusive Definition of the Small State," *International Politics* 46 (2009): 65–83; Björn G. Ólafsson, *Small States in the Global System: Analysis and Illustrations from the case of Iceland* (Aldershot, Hampshire, 1998); Commonwealth Secretariat, *A Future for Small States: Overcoming Vulnerability*, ed. Commonwealth Consultative Group (London, 1997).

[20] Tom Long, "It's Not the Size, It's the Relationship: From 'Small States' to Asymmetry," *International Politics* 54 (2017): 144–160; Mark P. Hampton, "Exploring the Offshore Interface: the Relationship Between Tax Havens, Tax Evasion, Corruption and Economic Development," *Crime, Law and Social Change* 24 (1995): 293–317.

[21] Peter J. Katzenstein, *Small States in World Markets: Industrial Policy in Europe* (New York, 1985); Paul Sutton, "The Concept of Small States in the International Political Economy," in *Small States in Multilateral Economic Negotiations*, ed. Amrita Narlikar (London/New York, 2016), 7–19.

[22] Godfrey Baldacchino, *Island Enclaves: Offshoring Strategies, Creative Governance, and Subnational Island Jurisdictions*, vol. 14 (Montreal, Quebec, 2010); Crowards, "Defining the Category."

[23] Commonwealth Secretariat, *Vulnerability: Small States in the Global Society*, ed. Commonwealth Consultative Group (London, 1985).

[24] Sheila Harden, *Small Is Dangerous: Micro States in a Macro World* (London, 1985).

[25] Alberto Alesina and Enrico Spolaore, "On the Number and Size of Nations," *The Quarterly Journal of Economics* 112, no. 4 (1997): 1027–1056; Alberto Alesina, "The Size of Countries: Does It matter?," *Journal of the European Economic Association* 1, nos. 2–3 (2003): 301–316; William Easterly and Aart Kraay, "Small States, Small Problems? Income, Growth, and Volatility in Small States," *World Development* 28, no. 11 (2000): 2013–2027.

reliant on international markets and alliances with larger states for security and economic support.[26]

Despite these challenges, historical evidence suggests that small states often achieve economic performance that surpasses mere survival.[27] Economically, they focus on export industries, preferably capital-intensive or service sectors that do not require high levels of labor.[28] Politically, they strive to develop "soft power" strategies, such as "opportunistic pragmatism" or "managed dependency," to navigate relationships with larger states and regional blocs, sometimes even developing forms of "symbiotic" partnership with them.[29] Thus, they leverage their smallness or the "power of being powerless" to foster their activities or interests, turning their position at the fringes of the international arena into an advantage.[30] This approach allowed several small states to act as "honest brokers" in international organizations, mediating conflicts and forging compromises to protect their interests.[31] It also helped some European countries, such as the Principality of Monaco, Luxembourg, Liechtenstein, and Malta, as well as larger ones, such as Switzerland, to grow their economies and globally enhance their political influence by adopting strategies that political scientist Ronen Palan defines as "bifurcation of sovereignty," namely the provision of less regulated and taxed areas within their sovereign jurisdictions.[32]

[26] Andrew Cooper and Timothy Shaw, *The Diplomacies of Small States: Between Vulnerability and Resilience* (New York, 2009); Michael W. Mosser, "Engineering Influence: The Subtile Power of Small States in the CSCE/OSCE," in *Small States and Alliances*, ed. Erich Reiter and Heinz Gärtner (New York, 2001), 63–84; Ronald Sanders, "The Fight Against Fiscal Colonialism: The OECD and Small Jurisdictions," *The Round* Table 91, no. 365 (2002): 325–348.

[27] Harvey W. Armstrong and Robert Read, "Comparing the Economic Performance of Dependent Territories and Sovereign Microstates," *Economic Development and Cultural Change* 48 (2000): 285–306; Easterly and Kraay, "Small States," 2014; Long, "It's Not the Size"; Robert L. Rothstein, *Alliances and Small Powers*, Institute of War and Peace Studies of the School of International Affairs of Columbia University (New York, 1968).

[28] Katzenstein, *Small States*; Vlcek, *Offshore Finance*.

[29] Alan Chong, "Singapore and the Soft Power Experience," in *The Diplomacies of Small States: Between Vulnerability and Resilience*, ed. Andrew Cooper and Timothy Shaw (New York, 2009), 65–80; Godfrey Baldacchino, "Bursting the Bubble: The Pseudo-Development Strategies of Microstates," *Development and Change* 24, no. 1 (1993): 29–52; Mark P. Hampton and John E. Christensen, "Treasure Island Revisited. Jersey's Offshore Finance Centre Crisis: Implications for Other Small Island Economies," *Environment and Planning A* 31, no. 9 (1999): 1619–1637; Tijn van Beurden and Joost Jonker, "A Perfect Symbiosis: Curaçao, the Netherlands and Financial Offshore Services, 1951–2013," *Financial History Review* 28, no. 1 (2021): 67–95.

[30] Baldacchino, "Bursting the Bubble," 39; Roger Bourbaki, "End of Paradise? Le Luxembourg et son secret bancaire dans les filets du multilatéralisme," *Critique internationale* 71 (2016): 55–71.

[31] Ole Elgström, "Introduction," in *European Union Council Presidencies: A Comparative Perspective*, ed. Ole Elgström (London, 2003), 1–17.

[32] Ronen Palan, "Trying to Have Your Cake and Eating It: How and Why the State System Has Created Offshore," *International Studies Quarterly* 42, no. 4 (1998): 625–643; Armstrong and Read, "Comparing the Economic Performance"; Vlcek, *Offshore Finance*; Richard Woodward, "From Boom to Doom to Boom: Offshore Financial Centres and Development in Small States," *SSRN* 1879298 (2011): 1-37.

Scholarship focusing on the role of country size in government and public administration has shown that a state's size impacts local institutions' development.[33] Small countries often exhibit "managed intimacy," a flexible approach to administrative regulations driven by close-knit communities and multi-functional roles.[34] Personal relationships hold significant importance, fostering interconnected networks where individuals wear different hats and relationships serve various purposes. This tight cohesion can enhance governance, promote information exchange among stakeholders, and encourage internal compromise and informal professional interactions.[35] Additionally, the smaller size of administrations compared to those of larger countries facilitates quicker execution and prioritization of key issues. However, this social cohesion might impair critical debate within the local community, leading to an overall acceptance of ethically questionable practices, such as economic specialization in offshore and tax avoidance services.[36]

According to political scientist Peter Katzenstein, small states often feature corporatist practices or "social corporatism," involving personal partnership in social and economic policy and "low-voltage politics," namely, the voluntary coordination of conflicting objectives through ongoing informal negotiation.[37] Additionally, small states frequently feature "peak associations," centralized, and concentrated interest groups that can significantly influence the government. This sheds light on why, although managed intimacy and multifunctionalism typically hinder specialization in smaller countries, some, such as Luxembourg, have cultivated a high level of professionalism by employing rare specialists and foreign experts. Specifically, the Grand Duchy's centralized system of competitive examinations provided additional support in this regard.[38]

Thus, Luxembourg's case complements many business history studies on the role of networks, experts, and corporatism in industry emergence, allowing us to investigate these dynamics in the context of a small state. A wealth of historical studies examined corporatism as a cooperative solution between business, labor, and government in large economies, such as Germany and the UK.[39] Other work focused on business-government cooperation in different contexts and in the EU integration process.[40] Historical research on "communities of experts" (also known as "epistemic

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33 Tiina Randma-Liiv, "Small States and Bureaucracy: Challenges for Public Administration," *Trames* 6, no. 4 (2002): 374–389.

34 David Lowenthal, "Social Features," in *Politics, Security and Development in Small States*, ed. Colin Clarke and Tony Payne (London, 1987), 26–49, here: 38–39.

35 Burton Benedict, *Problems of Smaller Territories* (London, 1967).

36 Mark P. Hampton and John Christensen, "Offshore Pariahs? Small Island Economies, Tax Havens, and the Re-Configuration of Global Finance," *World Development* 30, no. 9 (2002): 1657–1673 here: 1664.

37 Katzenstein, *Small States*, 32–33.

38 Jugl, *Country Size*, 62–63.

39 Philip Ollerenshaw, "Business, Politics and the Transition from War to Peace: The Federation of British Industries, 1916–25," *Business History* 67, no. 1 (2025): 126-146; Christian Marx and Morten Reitmayer, "Introduction: Rhenish capitalism and business history," *Business History*, 61 no. 5 (2022): 745–784.

40 Niklas Jensen-Eriksen, "Creating an Entrepreneurs' Movement: SME Associations as Political Actors in Late Twentieth-Century Finland," *Business History* (advance online publication, 7 May 2024), accessed 5 March 2025,—https://www.tandfonline.com/doi/full/10.1080/00076791.2024.2343870; Grace Ballor, *Enterprise and Integration: Big Business and the Making of the Single European Market* (Cambridge, UK,

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communities," "communities of interest," or "communities of practice") highlighted how these cohesive groups of professionals foster specialization within industrial districts, and clusters.[41] These communities generally share values and common goals, and may formalize their networks through associations and publications or maintain informal relationships through regular social gatherings.[42] They often emerge in specialized environments, such as science, academia, or business expat circles, and play a significant role in policy and international relations through lobbying.[43] Specifically, Waterhouse's analysis of the lobbying strategies that shaped policy outcomes in the USA and Coen and colleagues' assessment of the micro-scale lobbying practices in Europe, such as the systematic use of revolving-doors in lobbyist careers, significantly influenced our understanding of the mechanisms behind the emergence of mutual fund specialization in Luxembourg.[44]

In light of this multidimensional approach, the Grand Duchy presents an intriguing case of a corporatist system where a close-knit community of finance experts and legal professionals at the intersection of finance and politics influenced regulation at the national level and within the broader European context. Luxembourg's small size facilitated and reinforced the dynamics of knowledge exchange typical of dense expert communities. This led to the country's specialization in financial services and the growing sophistication of local tax avoidance practices.

Historical Materials and Use of Sources

The bulk of our analysis was based on primary data, historical material sourced from five physical archives in Luxembourg, Belgium, and Switzerland (Table 1 presents the specifics of archive materials): the Luxembourg National Archives (ANL) and the archives of the Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg; the National Archives (Archives Générales du Royaume, AGR) and the Belgium National Bank Archives (BNBA) in Belgium; and the Archives of Graduate Institute of International and Development Studies (AGI) in Switzerland.

2025); Gunnar Lind Haase Svendsen, "Associational Autonomy or Political Influence? The Case of the Cooperation Between the Danish Dairies' Buttermark Association and the Danish State, 1900–1912," *Business History* 56, no. 7 (2014): 1084–1110; Maiju Wuokko, "The Curious Compatibility of Consensus, Corporatism, and Neoliberalism: The Finnish Business Community and the Retasking of a Corporatist Welfare State," *Business History* 63, no. 4 (2019): 668–685.

41 Patrick Cohendet, David Grandadam, Laurent Simon, and Ignasi Capdevila., "Epistemic Communities, Localization and the Dynamics of Knowledge Creation," *Journal of Economic Geography* 14, no. 5 (2014): 929–954; Valeria Giacomin, "The Transformation of the Global Palm Oil Cluster: Dynamics of Cluster Competition Between Africa and Southeast Asia (c. 1900–1970)," *Journal of Global History* 13, no. 3 (2018): 374–398.

42 Ash Amin and Joanne Roberts, "Knowing in Action: Beyond Communities of Practice," *Research Policy* 37, no. 2 (2008): 353–369; Etienne Wenger, "Communities of Practice: Learning as a Social System," *Organization* 7, no. 2 (2000): 247–268.

43 Patrik Marier, "Empowering Epistemic Communities: Specialised Politicians, Policy Experts and Policy Reform," *West European Politics* 31, no. 3 (2008): 513–533; Amy Verdun, "The Role of the Delors Committee in the Creation of EMU: An Epistemic Community?," *Journal of European Public Policy* 6, no. 2 (1999): 308–328.

44 Benjamin C. Waterhouse, *Lobbying America: The politics of business from Nixon to NAFTA* (Princeton, NJ, 2013); David Coen, Alexander Katsaitis, and Matia Vannoni, *Business Lobbying in the European Union* (Oxford, UK, 2021).

Table 1. Detail of Archival Sources

Archive Name and Location	Data Overview
Archives Nationales de Luxembourg (ANL), Luxembourg	Chamber's debates, preparatory documents for laws, and Luxembourgish laws.
Archives de la Commission de Surveillance du Secteur Financier (CSSF), Luxembourg	Dossiers on funds (such as Eurunion fund and liquidation of IIT fund) and aggregate data on sales and redemptions of funds (1968–1977).
Archives Générales du Royaume (ARB), *Fonds Banque Lambert*, Bruxelles, Belgium	Dossiers and confidential documents on Eurosyndicat, Eurunion fund, Finance-Union fund, and Patrimonial fund.
Belgium National Bank Archives (BNBA), Belgium	Statistics on Luxembourg-domiciled funds, reports of analysts on characteristics of Luxembourg's market, proceedings of conferences on the subject, and advertising pamphlets for Luxembourg-domiciled funds.
Archives of Graduate Institute of International and Development Studies (AGI), Geneva, Switzerland	Collection of publications of Luxembourg Stock Exchange between 1929 and 1988.
Council of the European Union Archives (CEUA), Bruxelles, Belgium (online)	Collection of preparatory documents for the UCITS directive of 1985, transcripts of Council delegations' remarks, and final text of the directive.
EUI Historical Archives of the European Union (EUIHA), Firenze (Italy) (online)	Preparatory documents for a proposed directive on the taxation regulation of securities investments within the European Community.
FINLUX archive (curated by Matteo Calabrese, Alexander Davidov, Othmane Djebbar, Benoît Majerus, Christelle Timis and Luca Uhrig), C2DH, Luxembourg University, Luxembourg (online)	Data on more than 4600 Luxembourg-domiciled holding companies, banks, insurance firms, and law firms, with information on more than 15,800 individuals and firms involved as stakeholders, board members, notaries, lawyers, etc.
Legilux, Journal Officiel du Grand-Duché du Luxembourg, Luxembourg (online)	The official website of the Grand Duchy of Luxembourg dedicated to national legislation. The website provides access to Luxembourgish legislation published in the *Mémorial*, the Official Journal of the Grand Duchy of Luxembourg, which consists of two parts (Volumes A and B). A third part (Volume C) existed until 30 June 2016. (see https://legilux.public.lu/help/memorials)

In analyzing our sources, we adopted an abductive methodology involving continuous navigation between data and theory to infer the best explanation across multiple potential patterns of evidence.[45] While we presented the research outcome as a linear narrative, it was, in fact, a highly iterative process involving the application of the business history methodological "triad," further developed in recent literature, comprising hermeneutic cycle, contextualization (triangulation), and source criticism across the records.[46] This approach helped us compile a meticulous reconstruction of the development of the industry, identify the major actors, events, and dynamics of the time, and assess the most relevant context-specific meanings and concepts.[47]

The ANL and CSSF archives provided statistical and qualitative information on Luxembourg's fund market, including internal reports, fund prospectuses, advertising, and dossiers on liquidated funds. The AGI archives at the Graduate Institute of Geneva offered publications from the Luxembourg Stock Exchange (1929–1988), which helped to track the industry's growth. The BNBA archives supplied insights into Belgian and Luxembourgish funds, technical assessments, and a collection of legal sources, shedding light on the relationship between both countries' financial sectors. As a major shortcoming, these sources lacked investor details and information on the drafting of local mutual fund regulations. To fill this gap, we triangulated our findings by consulting four online collections: the *Journal Officiel du Grand-Duché du Luxembourg*, the Council of the European Union Archives (CEUA), the European University Institute Historical Archives, and the FINLUX database. Although some aspects of the drafting process and several involved actors remain concealed, these collections provided legal texts, drafts, parliamentary debates, and data on over 4600 companies and 15,800 individuals, allowing us to better reconstruct and map the connections between the involved financial intermediaries and Luxembourg's policymakers.

To address the limitations in our primary sources, we complemented our analysis of archival material with "grey" or supporting literature available online, including articles from contemporary newspapers and publications from business-law firms, which provided a more granular view of the relationships between financiers and lawmakers and shed light on the internal dynamics and shared values of the industry. For instance, following the 1972 "IOS scandal," which implicated Luxembourg's primary fund provider, terms such as "disbelief" and "disillusion" were prevalent in

[45] Igor Douven, "How Explanation Guides Belief Change," *Trends in Cognitive Sciences* 25, no. 10 (2021): 829–830; Alf Steiner Sætre and Andrew Van de Ven, "Generating Theory by Abduction," *Academy of Management Review* 46, no. 4 (2021): 684–701.

[46] R. Daniel Wadhwani, Matthias Kipping, and Marcelo Bucheli, "Analyzing and Interpreting Historical Sources: A Basic Methodology," in *Organizations in Time*, ed. Marcelo Bucheli and R. Daniel Wadhwani (Oxford, 2013), 305-329; Sandeep D. Pillai, Brent Goldfarb, and David A. Kirsch, "Lovely and Likely: Using Historical Methods to Improve Inference to the Best Explanation in Strategy," *Strategic Management Journal* 45, no. 8 (2024): 1539–1566; R. Daniel Wadhwani and Stephanie Decker, "Clio's Toolkit: The Practice of Historical Methods in Organization Studies," in *The Routledge Companion to Qualitative Research in Organization Studies*, ed. Mir Raza and Sanjay Jain (London/New York, 2017), 113–127.

[47] Gino Cattani, Simone Ferriani, and Andrea Lanza, "Deconstructing the Outsider Puzzle: The Legitimation Journey of Novelty," *Organization Science* 28, no. 6 (2017): 965–992.

the local press.[48] This language revealed a societal distrust that was not immediately apparent from quantitative and legal sources alone.

Finally, between 2021 and 2023, we conducted three in-depth oral history interviews with prominent figures in Luxembourg's financial industry and political sphere. These included Jacques Santer, former Prime Minister and Minister of Finance; Jeanne Chèvremont, an economist specializing in Luxembourg's financial market; and Claude Kremer, a Luxembourgish legal expert on investment funds.[49] These interviews were crucial in filling gaps in the archival material, and in gaining a deeper understanding of the fund industry's evolution during the 1970s and 1980s. Through triangulation and cross-checking of information, we could capture perspectives and rationales often difficult to discern from archival sources alone. Santer and Chèvremont, in particular, provided insights into the collaboration between experts and government representatives during the drafting of Luxembourg's mutual fund legislation in the 1980s. Together, these interviews offered a more nuanced and insider perspective on the development of the financial mechanisms that shaped the industry.

Business-Government Nexus Underpinning the Birth of Luxembourg's Mutual Fund Industry, 1940s–1950s

Since its inception in 1959, Luxembourg's mutual fund industry has been characterized by a close relationship and often overlap between its political and financial elites, hinging on a series of gradually established practices arising from this cooperation.

During the interwar period, the government and the majority party, the Parti de la Droite (which would later become the Christian Social People's Party (CSV)), actively supported and prioritized the country's economic specialization in financial services, setting the legal premises that would allow the mutual fund industry to emerge and consolidate after the war. In July 1929, Luxembourg's Parliament passed the controversial "Holding Act" (H29), overhauling the fiscal regime for locally registered holding companies.[50] This law granted complete exemption from interest and dividends taxes, and imposed the lowest capital stock taxation rate in Europe for such companies at that time.[51] Additionally, it proposed equal fiscal treatment for holding

[48] Ernest Muhlen, "Les fonds d'investissement au Luxembourg. Les investisseurs sont devenus plus circonspects," *Luxembourger Wort*, 18 March 1978, 25.

[49] Guy Thewes, *Les gouvernements du Grand-Duché de Luxembourg depuis 1848*, vol. Service information et presse du gouvernement Luxembourgeois, Département edition (Luxembourg, 2006), 193. After serving as Finance Minister from 1979 to 1984, Santer became the Prime Minister, and Minister of Finance in the subsequent coalition government of the CSV, and the Luxembourg Socialist Workers' Party (LSAP) until 1989. Jeanne Chèvremont, interview with the authors, 23 Nov. 2022. She worked as a specialist in Luxembourg's financial market for the audit company Coopers & Lybrand (then merged with Price Waterhouse, to form the current "big four" PwC) since the second half of the 1970s and then became a partner in 1987. Claude Kremer, Interview with the authors, 11 Jan. 2023. Kremer wrote an all-encompassing scholarly treaty on the modern jurisprudence of investment funds in Luxembourg, who, from 1981 to 1985, was a young practitioner at Elvinger & Hoss, a major Luxembourg law firm specializing in funds.

[50] *Session ordinaire de la Chambre des Députés 1928–1929 (Compte rendu des séances publiques)*, box CR-0129, Chambre des Députés (CdD), Archives nationales de Luxembourg (ANL).

[51] Calabrese and Majerus, "Archaeology."

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companies and investment trusts. The latter, precursors to modern closed-end funds, differed from mutual funds because they had a fixed supply of shares and did not offer direct redemptions.

As shown by Calabrese and Majerus, from the 1930s, Luxembourg's holding system already featured a strong presence of overlapping roles and recourse to revolving-door practices, with the same individuals occupying different positions or switching between lawmakers and lobbyists for the financial industry. Although the idea for drafting a law on holding companies most likely came from the legal department of Luxembourg's leading steel conglomerate Aciéries Réunies de Burbach-Eich-Dudelange (ARBED), several members of the Parti de la Droite were also deeply involved in the country's holding system.[52] They served as notaries, administrators, or stakeholders while simultaneously holding seats in Parliament. For instance, Auguste Thorne, one of the party's most prominent members, was also on the Ford Investment Company board, a holding company established in 1930 in Luxembourg by the American automotive company to minimize its taxes in Europe.[53] Others, instead, benefited from their prior government involvement, leveraging their connections within the Parti de la Droite to advance their careers in law and notary firms after leaving Parliament. This was the case for Edmond Reiffers, one of Luxembourg's most active notaries in listing new holding companies since the end of 1929.[54] Before focusing entirely on his notary firm, he had served as Minister for Finances and Public Education in the 1910s for the Parti de la Droite.[55]

The holding system proved highly efficient in several respects, particularly by helping the state mitigate the effects of the Great Depression by providing an alternative source of revenue for the state budget through capital taxes on holding companies when overall state fiscal income was declining.[56] The profitability of this system likely contributed to its survival and continuity during the Nazi occupation of Luxembourg (1940–1945).[57] Although evidence on corporate management under German occupation is limited, only about 20% of the country's holding companies

[52] Calabrese and Majerus, "Archaeology," 3. ARBED ultimately decided against creating a holding company. The official reason, as reported to the press, was that the 1929 financial crisis had caused the company to reconsider its plans owing to the worsening economic climate. Interestingly, under the leadership of its head of legal affairs, Léon Metzler, ARBED launched a public campaign against the holding law in the Luxembourgish press in the early 1930s. ARBED's vocal criticism of the "abuses of the law" could be seen as a response to the company's dissatisfaction with the government's efforts. The company had sought stronger measures, including further reductions or even the elimination of annual capital stock taxes on holding companies, as revealed in a letter ARBED sent to the Luxembourg Tax Authority during the law's preparatory phase in 1929 (*Projet de loi sur le régime fiscal des sociétés de participations financières dites holding companies (1929–1937)*, proposed amendments to the Holding Act by Deputy M.H. Clement, February 1937, box 2467, Conseil d'État, ANL; *Réformes concernant les différents droits et taxes fiscales ainsi que relevés et avis y relatifs, 1907–1929*, letter from ARBED, 10 May 1929, box 3788, Administration de l'Enregistrement et des Domaines, ANL.

[53] Calabrese and Majerus, "Archaeology," 13–14.

[54] Calabrese and Majerus, "Archaeology," 10.

[55] Legilux, *Arrêté grand-ducal du 22 janvier 1916, accordant démission honorable à M. Edmond Reiffers, directeur général des finances et de l'instruction publique.*

[56] Calabrese and Majerus, "Archaeology," 9.

[57] Calabrese and Majerus, "Archaeology," 17.

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(such as Ford Investment) and investment trusts (such as Union Internationale de Placements) listed before the war relocated or de-registered as a result of the occupation, often owing to their stakeholders being Jewish or of nationalities hostile to Germany.[58] The German occupiers tightened control over the financial sector but likely saw the fiscal benefits for the state budget of H29, and left it unchanged, allowing a core group of Luxembourgish holding companies to remain active.[59] The German authorities also maintained continuity in tax collection, with Conrad Stumper, head of the Administration of Registration and Domains since 1930, continuing in his role through the war and until 1948.[60]

After the war, the holding system was thus still in place, albeit significantly downsized by the conflict.[61] However, through the 1950s, the number of listed holding companies in Luxembourg began to rise again, alongside deeply entrenched practices, such as occupying overlapping roles and engaging in revolving-door activities.[62] These practices would soon become defining features of Luxembourg's upcoming mutual fund industry.

Specifically, the notary and business lawyer Bernard Delvaux played a pivotal role in developing and establishing the mutual fund industry in Luxembourg. Delvaux had been one of the primary architects behind the previous phase of Luxembourg's financial development, specifically through the introduction of the Holding Act. He began his apprenticeship at Edmond Reiffers' notary firm in the early 1930s, where he quickly developed expertise in holding company legislation, particularly regarding the forms of legal continuity between holding companies and investment trusts.[63]

From its inception, the preparatory documents of H29 granted that the financial assets within a holding company's portfolio could take "any form," including "shares, stocks, bonds, and so on."[64] The Act thus provided investors and shareholders with a legal framework for establishing investment trusts, enabling pooled investments in securities traded on secondary financial markets without direct recourse to parent-subsidiary management or profit-and-loss consolidation strategies, as was typical with traditional holding companies.[65] In 1933, Delvaux, in collaboration with Reiffers,

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58 FINLUX Database; Bernard Delvaux, "Questions actuelles concernant la loi du 31 juillet 1929 sur le régime fiscal des sociétés de participations financières," *Pasicrisie Luxembourgeoise* (1956): 145-65 here: 14–16.

59 See in particular the case of German banker and financier Hermann Josef Abs, who was unilaterally appointed by the German occupiers as managing director of Luxembourg's BGL bank during the occupation. He had previously been involved as executive director with two Luxembourg holding companies, Société d'Électricité Sodec S.A. and Luxemburger Unionbank S.A., between 1936 and 1938 (FINLUX Database).

60 *Budget de l'exercice 1941*, box 00304, Administration de l'Enregistrement et des Domaines, ANL; Legilux, *Arrêté grand-ducal du 19 avril 1930 concernant la fixation des salaires dus aux conservateurs des hypothèques*; *Bulletin d'Information*, Grand-Duché de Luxembourg, Ministère d'Etat, accessed 6 Jan. 2025, https://sip.gouvernement.lu/dam-assets/publications/bulletin/1948/BID_1948_1/BID_1948_1.pdf.

61 Eric Eich, "La législation holding et son impact sur l'économie luxembourgeoise," in *Mémoire de licence* (UCL1979), 36.

62 STATEC, *Statistiques Historiques 1839–1989* (Luxembourg, 1990), 351.

63 J.G., "In Memoriam Bernard Delvaux," *Luxemburger Wort*, 8 April 1972.

64 *Projet de loi sur le régime fiscal des sociétés de participations financières dites holding companies (1929–1937)*, M-02467, Conseil d'État, ANL. Authors' translation from French.

65 Calabrese and Majerus, "Archaeology." 13.

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coauthored a seminal monograph on the interpretation of H29, focusing on the relationship between holding companies and investment trusts. This work gained immediate approval and official acknowledgment from Luxembourg's tax administration. The publication displayed the subtitle "Reviewed by the Directorate of the Administration of Registration and Domains" on its opening pages, indicating that Delvaux and Reiffers' interpretation of the matter could be considered official.[66]

In the post-war period, Delvaux built upon this legal foundation to explore the continuity and fiscal equivalence between investment trusts and mutual funds. The preparatory documents of H29 envisaged the organization of investment trusts as holding companies but remained silent on extending the same regulatory framework to mutual funds. Delvaux's innovative interpretation argued instead that mutual funds, such as investment trusts and holding companies, could benefit from zero tax on interest and dividends (including withholding taxes), and enjoy the same low capital stock tax rates. This interpretation hinged on the condition that their management companies, responsible for managing a portfolio in undivided co-ownership, were registered in Luxembourg as holding companies.[67] Thus, this framework allowed mutual funds to be subject to H29 while maintaining their primary features of modern open-ended funds, namely an elastic supply of shares, provisions for direct refunds upon redemption by the fund management company and the separation of liabilities between the fund's investors and fund managers.[68]

Delvaux's expansive interpretation of the H29 exemplifies what legal scholar Katharina Pistor provocatively defined as the lawyer's "code mastery."[69] This refers to the ability of business lawyers, acting as financial intermediaries, to craft new legal precedents by creatively interpreting existing legislation and securing approval from national regulatory bodies. We define this strategy as a "dynamic interpretation" of existing laws. This practice, in turn, was pivotal in furthering the "bifurcation of the sovereignty" through which Luxembourg was building its comparative advantage as an international offshore platform for holding companies and funds.

Besides his work as a notary in Reiffers' firm throughout the 1930s, Delvaux had also sat on the boards of multiple holding companies domiciled in Luxembourg, such as the Continental Finanz und Placierungs Gesellschaft and the Société de Participations Financières, Industrielles et Commerciales (of whom he was the managing director). He was also on the executive board of Luxembourg-based Banque Mathieu Frères.[70] Additionally, from 1945, he had continuously been part of one of the early boards advising Luxembourg's national financial regulator, Commissariat au Contrôle de Banques (CCB), on matters related to investment in financial securities.[71]

[66] Bernard Delvaux and E. Reiffers, *Les Sociétés "Holding" au Grand-Duché de Luxembourg: Etude théorique et pratique de la loi du 31 juillet 1929* (Luxembourg, 1933).

[67] Delvaux, "Questions actuelles concernant la loi du 31 juillet 1929 sur le régime fiscal des sociétés de participations financières"; Bernard Delvaux, "Les Sociétés d'Investissement du type ouvert au Grand-Duché de Luxembourg," *Pasicrisie Luxembourgeoise* XVIII (1961): 37–85.

[68] Morley, "The Separation of Funds and Managers."

[69] Pistor, *The Code of Capital.*

[70] FINLUX Database.

[71] FINLUX Database.

Delvaux's ideas on mutual funds gained traction throughout the 1950s, initially in Luxembourg, where he published two articles in a local law journal.[72] His influence soon extended to neighboring Belgium, where Banque Lambert, a bank with a strong international orientation, was making its early moves in the global mutual fund market.[73] In 1959, Banque Lambert added another role to Delvaux's portfolio by hiring him as its representative in Luxembourg. This appointment was part of the bank's project to establish a group of mutual funds in Luxembourg, including the Eurunion fund in 1959 and the Patrimonial fund in 1960.[74] Internal documents from Banque Lambert indicate that the bank, seeking a more fiscally advantageous fund market than Belgium, found reassurance in Delvaux's extensive knowledge of the Luxembourg financial sector.[75] This experience stemmed from his direct involvement as a business lawyer, notary, and director of holding companies and his strong connection with the CSV party, which had regained control of Parliament and the government after the war.

As Banque Lambert's emissaries reported in a confidential document addressed to the board of directors,[76] Delvaux assured that he had obtained direct guarantees from Luxembourg's Ministry of Finance and registration authorities regarding the approval of his broad interpretation of H29 for mutual funds. Furthermore, he asserted that formal approval from Luxembourg's Parliament was "of no practical importance" to this purpose.[77] Delvaux's forecast proved accurate: the Ministry of Finance, led by CSV member Pierre Werner and the Administration of Registration and Domains, indeed effectively granted de facto approval to Delvaux's proposal with the listing of the Eurunion fund in February 1959, the first mutual fund listed in Luxembourg.[78]

In sum, starting from the 1950s, the business and political elites of the Grand Duchy of Luxembourg laid the basis for the emergence and strengthening of a national mutual fund industry. Two main strategies underpinned the financial specialization of the Grand Duchy and would continue to shape the industry in the decades ahead. First, the widespread practice by the local community of legal and business professionals specializing in finance to hold overlapping roles or resort to revolving-door strategies to foster their careers. Specifically, Luxembourg elites operated in a dense network at the intersection of business and politics, typical of small states' governance. Second, the refinement of the dynamic interpretation of existing laws, particularly the Holding Act of 1929, de facto allowed mutual funds' management companies to be listed in Luxembourg as holding companies, thus benefiting from the same advantageous fiscal conditions. This further opened the way for the Grand Duchy to become a prime destination for tax avoidance.

[72] Delvaux, "Les Sociétés"; Delvaux, "Questions actuelles concernant la loi du 31 juillet 1929 sur le régime fiscal des sociétés de participations financières."

[73] Paul Smets, *Lambert. Une aventure bancaire et financière* (Bruxelles, 2012).

[74] *Fonds Liquidé Eurunion, 1966–1978 III Anc.L., Extrait du Mémorial (Recueil Spécial) – Luxembourg national business register* – no. 17, 19 March 1959; no. 84, 22 Dec. 1959, box 13934, CSSF; *Fond Patrimonia [sic]*, box 4920, Banque Lambert, Archives générales du Royaume (AGR).

[75] *Note pour Monsieur Thierry*, 15 March 1960, box 4918, fonds Patrimonia [sic], Banque Lambert, AGR.

[76] *Note pour Monsieur Thierry, "Question fiscale,"* 15 March 1960, box 4918, AGR.

[77] *Note pour Monsieur Thierry*, 15 March 1960, box 4918, AGR.

[78] Delvaux, "Les Sociétés," 67.

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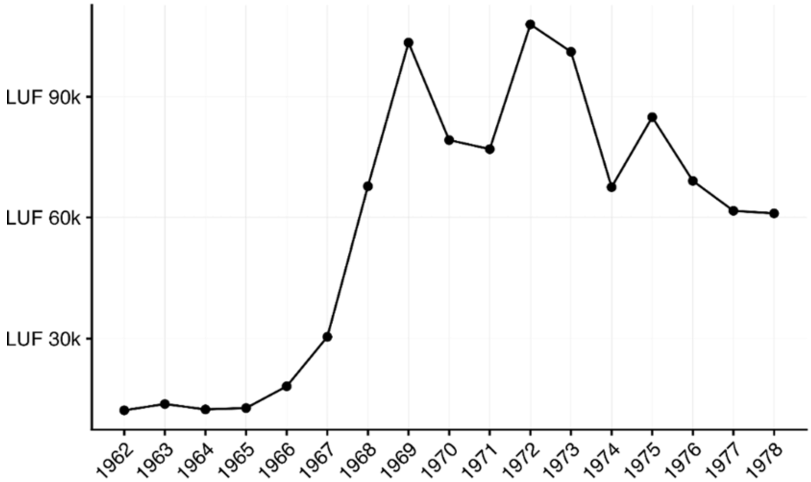

Figure 1. Aggregate capital stock of Luxembourg's mutual funds (LUF million), 1962–1978, (adjusted for inflation, reference year 1978). (Source: Les Fonds de placement au Grand-Duché de Luxembourg, April 3, 1967, Department of Studies, Information Service, box 1529/9, BNBA; CMoW SEQ Luxembourg, Luxembourg Stock Exchange Publications 1967–1978, 4.16.1, AGI; Bulletins trimestriels 1, CSSF. Authors' calculations.)

Business-Government Nexus in Early Internationalization of Luxembourg's Mutual Fund Industry, 1960s– 1970s

Between the 1960s and 1970s, Luxembourg's fund industry soared in terms of aggregate assets and interactions with international fund management companies and non-resident investors. As shown in Figure 1, between 1962 and 1978, the aggregate capital stock of all mutual funds listed in LuxSe grew from approximately 10 billion Luxembourg francs (LUF) to around 60 billion, peaking at LUF 110 billion in 1972.

Since the 1950s, Pierre Werner had been rising as a central figure in the internationalization of Luxembourg's *place financière.* A member of the CSV party, he had been a close collaborator of the late Pierre Dupong, one of the minds behind the promulgation of the Holding Act in 1929 and Luxembourg's Prime Minister, until his sudden death in 1953.[79] After being Commissioner of CCB during the 1950s, Werner became *ad interim* Prime Minister and Minister for Finance in March 1959.[80] Werner later recalled that the decision to approve the listing of mutual funds in Luxembourg in 1959 was primarily rooted in a tradition of "dynamic interpretation" of the Holding Act.[81] He also emphasized that the approval aimed to lay the groundwork for further internationalization of Luxembourg's financial sector. These developments occurring in the absence of a Central Bank allowed for greater flexibility in centralized supervision of the financial industry, enabling fund

[79] Calabrese and Majerus, "Archaeology."

[80] Thewes, *Les gouvernements*, Service information et presse du gouvernement Luxembourgeois, Département edition, 141–153.

[81] Pierre Werner, *Les organes collectifs de placement dans la perspective de la place financière de Luxembourg : journées d'études – 11 et 12 décembre 1970* (Luxembourg City, 1971). See the foreword, 3–4.

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managers and banking intermediaries to transact freely in various currencies without any "concern for [Luxembourg's] monetary prestige."[82] This was especially relevant for a country, such as the Grand Duchy, which had been in a monetary union with Belgium since the 1920s. The Belgo–Luxembourgish monetary union further facilitated the initial expansion of the Luxembourg mutual fund industry northward alongside the Belgium axis.[83]

Just 1 year before the listing of the Eurunion fund, Brussels-based Banque Lambert had founded a network of inter-European banks known as Eurosyndicat. Besides Banque Lambert itself, this included six banks from the European founding member states, and together with the Paris-based Société Financière et Mobilière, they were also the first shareholders of the Eurunion fund in 1959.[84] Six more banks from Luxembourg, the UK, Switzerland, and Germany would eventually join Eurosyndicat in the 1960s.[85] In its annual reports from the 1960s, the Eurosyndicat advertised a financial market strategy centered on network-level information sharing to achieve economies of scale and diversification of investment policies through collectively managed, high-performing mutual funds.[86] Thus, Luxembourg's financial industry initially focused on business-to-government relationships and later expanded its business-to-business nexus under Banque Lambert's leadership.

Banque Lambert's analyses, shared with other Eurosyndicat members, identified Luxembourg as the most advantageous mutual fund issuing platform in Europe for international investors, primarily due to "fiscal reasons."[87] Banque Lambert's analysts soon assessed that:

> [. . .] although in Belgium we have legislation [on open-end funds] which has proved to be satisfactory on the whole, there is an obstacle hindering attempts

[82] *Conférence de Pierre Werner sur le Luxembourg et les euro-marchés (Luxembourg, 5 octobre 1982)*, 5, accessed 6 Jan. 2025, https://www.cvce.eu/content/publication/2013/10/30/1e983235-d538-4001-9447-12c833618847/publishable_fr.pdf.

[83] During this crucial phase of further financialization, Luxembourg maintained a 1:1 parity between the Luxembourg franc and the Belgian franc, de facto outsourcing monetary policy to Belgium. Gilbert Trausch, *Belgique – Luxembourg: Les relations belgo-luxembourgeoises et la Banque générale du Luxembourg (1919–1994)* (Luxembourg, 1995).

[84] These banks were: the Compagnie d'Outremer pour l'Industrie et la Finance in Belgium; the Rothschild brothers' Crédit Commercial de France (Paris) and the Compagnie Financière in France; Berliner Handelsgesellschaft (Frankfurt) in Germany; Pierson, Heldring & Pierson (Amsterdam) in the Netherlands; and Banca Commerciale Italiana (Milan) through its branch Banca di Credito Finanziario "Mediobanca" in Italy. See: *Fonds Liquidé Eurunion, 1966–1978 III Anc., Extrait du Mémorial (Recueil Spécial) – Luxembourg national business register – no. 17*, 19 March 1959, box 13934, CSSF.

[85] These new banks included Banque Européenne in Luxembourg, the banks N.M. Rothschild & Sons (London) and Hill and Samuel & Co. Ltd. (London) in the UK, Banque Privée (Geneva) in Switzerland, Bayerische Staatsbank (Munich) in Germany, and Banca Provinciale Lombarda (Bergamo), replacing Mediobanca as the Italian representative in the early 1970s. See: *Fonds Liquidé Eurunion, Fusion avec Finance Union 1966–1978 II Anc. L, Prospectus d'émission 1968–1975*, box 13935, CSSF.

[86] *Eurosyndicat (1975–1976)*, 6, box 1225, Banque Lambert, AGR.

[87] *Note pour le conseil de la Sogim of R. L. Larcier (addressed to Marcel Decleve)*, 1 Feb. 1960, box 4918, Banque Lambert, AGR.

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> to create mutual funds of a "European nature" within this legal framework, those whose shares would be distributed in several countries [. . .]: taxation.[88]

Belgian bankers found themselves unable to influence mutual fund legislation in their own country, which at the time was enveloped in the public and state-level debate over the "execrable practice" of benefiting from tax evasion through Belgian capital investments in Luxembourg via holding companies.[89] Additionally, Belgian fund management companies were subjected to the same tax regime as ordinary commercial entities and faced higher fund registration costs than their Luxembourg counterparts.[90]

One of the first initiatives of Eurosyndicat was to readdress their international fund investors towards the group of mutual funds that the banking network had meanwhile incorporated in Luxembourg between 1959 and the early 1960s.[91] The Eurosyndicat served as a conduit linking the ideas emerging within the community of financial intermediaries and government officials in Luxembourg, centered around the holding and mutual fund sectors and the burgeoning European, and subsequently global markets of fund managers, and investors. Marcel Declève, a Belgian financial analyst serving as a key director both at Banque Lambert and in Eurosyndicat, rose as an influential figure representing the initial shift of the Luxembourg mutual fund industry from a primarily Belgo–Luxembourgish focus to an international one. Declève held decisional positions on the boards of Eurosyndicat's Luxembourg-domiciled funds, where Bernard Delvaux was involved as legal representative, such as Eurunion, Patrimonial, and Finance-Union.[92] Simultaneously, throughout the 1960s, he acted as board president or director in several financial bodies connected to the galaxy of Banque Lambert and Eurosyndicat, including the investment management companies Soges, Sogim, and Fiducem.[93]

Beyond the Eurosyndicat, the Grand Duchy's reach as a major financial hub expanded also overseas. At least initially, Banque Lambert remained at the center of this process. Owing to its prominent position as a mutual fund developer in Luxembourg, in 1960, the bank was approached by the Panama-based Investors Overseas Service (IOS) organization, an emerging key player in the global fund industry. IOS managed over 60 companies and mutual funds worldwide, primarily based in tax havens, such as Panama, the Bahamas, and the Netherlands Antilles.[94]

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[88] *Note pour le conseil de la Sogim*, 1 Feb. 1960, box 4918, AGR.

[89] *Législation belge relative aux sociétés holding étrangères et problèmes avec les sociétés holding luxembourgeoises* (28 Feb. 1955), "Les holdings belges et le fisc," *Le Soir*, box FIN-10661, ANL; *Législation belge relative aux sociétés holding étrangères et problèmes avec les sociétés holding luxembourgeoises*, "Projet de loi belge affectant le régime fiscal des entreprises dépendant de sociétés holding," December 1953, box FIN-10661, ANL.

[90] Bernard Delvaux, "Régime fiscal des sociétés d'investissement et des fonds communs de placement dans les pays de la C. E. E.," *Pasicrisie luxembourgeoise* (1963): 41–58 here: 53-54.

[91] This group of Luxembourg-domiciled mutual funds included the Eurunion fund and two other mutual funds: the Finance-Union fund and the Patrimonial fund (*Soges, Procès-verbaux des séances du conseil d'administration. Session of 22 June 1965, Dissolution du Fonds International de Placement (FIP)*, box 39532, Banque Lambert, AGR).

[92] *Rapport annuel 1963/64, Finance-Union*, box 4929, Banque Lambert, AGR.

[93] *Sogès, Exercice 1966*, 2, box 1187, Banque Lambert, AGR; *Note pour le conseil de la Sogim*, 1960, box 4918, Banque Lambert, AGR; *Sogès-Fiducem, Rapport de l'exercice 1978*, box 1196, Banque Lambert, AGR.

[94] Majerus, "This Is Not a Scandal."

Luxembourg's minimal taxation for fund management companies, the absence of withholding tax on international investors' gains from mutual funds and the light financial supervision environment created ideal conditions for IOS to establish mutual funds in the Grand Duchy.

The IOS contact likely reached Marcel Declève's desk around 1960. Banque Lambert initially agreed to support the IOS but ultimately withdrew before registering the IOS's first fund in Luxembourg, the IIT fund, in February 1961.[95] This decision was likely influenced either by their first-hand knowledge of the risky financial operations of IOS's flamboyant president, Bernard Cornfeld, and his questionable philosophy of "people capitalism," or, as described by Raw et al. in their popularized account of Cornfeld's saga, simply because they did not fully trust IOS's "unconventional approach."[96]

As a next step, the IOS organization opted to gradually embed itself within Luxembourg's dense network of financial intermediaries and political circles, often interconnected through familial ties. IOS was represented in the Grand Duchy by the Dupong law firm, established under the patronage of former Luxembourg Prime Minister Pierre Dupong. By the early 1960s, Pierre's two sons, Jean, who also served as a member of Luxembourg's Chamber of Deputies for CSV, and Lambert, led the Dupong law firm.[97] Lambert Dupong was also the legal representative for Fonditalia, the second-largest mutual fund in the IOS portfolio in Luxembourg, from 1967.[98]

Lambert Dupong garnered Pierre Werner's support for the IOS organization throughout the 1960s. Werner, as seen, had established himself politically under the tutelage of Pierre Dupong in the 1950s and consistently backed the Dupong law firm amidst conflicts between its client IOS and the CCB. At that time, the CCB oversaw the listing and advertising of mutual funds in Luxembourg amidst the country's mild regulatory screening for fund managers.[99] The CCB sought to leverage its minimal control prerogatives to gain greater oversight over IOS's speculative and opaque practices. However, as interim Minister of Finance, Werner had the last word on these regulatory matters and decided to side with the Dupong firm and advocate for non-interference in IOS's activities.[100] Werner defended some IOS practices that CCB

[95] *Liquidation du fonds IIT*, box 16656, CSSF.

[96] Bernie Cornfeld; Ran Ill-Fated IOS Fund," *Los Angeles Times*, 1 March 1995, L.A. Times Archives; Diana B. Henriques, "Bernard Cornfeld, 62, Dies. Led Flamboyant Mutual Fund," *New York Times*, 2 March 1995; Majerus, "This Is Not a Scandal." Charles Raw, Godfrey Hogson, and Bruce Page, *Do You Sincerely Want to Be Rich? Bernard Cornfeld and IOS: An International Swindle* (London, 1971), 85.

[97] FINLUX Database; Majerus, "This Is Not a Scandal."

[98] *FONDITALIA 9.85–5.86*, box 3630, CSSF; *CMoW SEQ Luxembourg, LuxSE Publications 1967–1978*, 4.16.1, Archives of Graduate Institute of International and Development Studies (AGI).

[99] *Arrêté grand-ducal du 19 juin 1965;* Circular letter of the Banking Control Commissioner no. VM/8 of 21 Dec. 1967 (regarding information to be produced in connection with the public display, offering, or sale of shares of mutual funds, or in connection with the application for listing of said shares on the Stock Exchange); Chapter V, arts. 26–36 of the Internal Rules of the LuxSE (formalities on admission of shares). See also Edmond Israel, "Luxembourg: The Taxation and Legal Regime of Investment Funds and Investment Companies," *European Taxation* 10, no. 8 (1970): 193–201 here: 201.

[100] *FONDITALIA 9.85–5.86*, letter of Ministry of Finance (signed by Pierre Werner) to Lambert Dupong, 4 Dec. 1968, box 3630, CSSF.

officials had harshly criticized, including the high commissions enjoyed by IOS fund managers in Luxembourg and the controversial policy of assigning liability to fund administrators (who could be "just strawmen") rather than the actual promoters. Werner framed these decisions as IOS's "free choice," and, contradicting the CCB's opinion, he approved the listing of IOS's Fonditalia in 1967 and 1968 as Minister of Finance.[101]

Throughout the 1960s until 1974, when CSV lost the general elections in Luxembourg to a centrist–socialist coalition, Werner, in his capacity as both Prime Minister and leader of CSV, strongly "resisted" and "passionately" supported subsequent applications of a dynamic interpretation of the Holding Act to mutual funds and progressively to another financial product: Eurobonds.[102] Luxembourg's financial legislation on holding companies, which had formed the foundation for its mutual fund industry, provided a favorable environment to apply its advantageous tax conditions to the growing Eurobond market—i.e., international bonds issued in a currency different from the issuer's home country, typically offered in bearer form, allowing for investor anonymity. According to financial historian Catherine Schenk, the Eurodollar market had already begun to develop in London by the mid-1950s.[103] Yet, it was in July 1963 that the release of US Regulation Q prompted the issuance of the first Eurobond by the Italian state company "Autostrade per l'Italia" through the LuxSe.[104]

Besides streamlined listing procedures compared with other markets, such as the London Stock Exchange (LSE), two applications of the dynamic interpretation of the Holding Act were crucial for choosing LuxSE as a nodal Eurobond platform.[105] First, Eurobonds issuers, like mutual funds, using holding companies as issuance vehicles, could benefit from the tax exemptions on dividends and interest in a regime of zero withholding taxation. Second, mutual fund shares and Eurobonds were issued as "bearer form" certificates, ensuring purchaser anonymity and facilitating tax evasion by hiding ownership from tax authorities.[106] The cohesion of the political and financial elites in the small Luxembourgish society favored a general acceptance of the misuse of these financial instruments for tax evasion purposes. This attitude is well exemplified by Werner when commenting on a European Commission's draft proposal for legislative harmonization in the member country's fiscal frameworks in 1968:

> [. . .] The majority of the experts' proposals were likely to disrupt our financial legislation profoundly, some elements of which have been the foundation of Luxembourg's success as an international financial center.

[101] *FONDITALIA 9.85–5.86*, letter of Ministry of Finance (signed by Pierre Werner) to Albert Dondelinger, 14 Oct. 1967, box 3630, CSSF.

[102] Pierre Werner, *Itinéraires luxembourgeois et européens. Evolutions et souvenirs: 1945–1985*, 2e éd., revue et corrigée ed., vol. II (1992), 97–98.

[103] Cathrine R. Schenk, "The Origins of the Eurodollar Market in London: 1955–1963," *Explorations in Economic History* 35, no. 2 (1998): 221–238.

[104] Gilbert Trausch and Marianne de Vreese, *Luxembourg et les banques: de la révolution industrielle au 7e centre financier mondial* (Luxembourg, 1995); Schenk, "The Origins," 222; Cassis, *Capitals*; Ogle, "Archipelago."

[105] Trausch and de Vreese, *Luxembourg et les banques*; Ogle, "Archipelago."

[106] Ogle, "Archipelago."

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This, as he candidly acknowledged:

> [although Luxembourg's holding and fund legislation] led, in some cases, to tax evasion, or even outright fraud.[107]

In summary, during the 1960s and 1970s, Luxembourg experienced a gradual internationalization as a hub for mutual funds. It first extended its influence to Belgium, where local bankers and financial intermediaries could not push for further tax exemptions in domestic mutual fund legislation. It then broadened its reach across Europe and overseas markets by strengthening business-to-government and business-to-business relationships. At the European level, the Eurosyndicat banking network helped Luxembourg promote its fiscally convenient mutual funds across the European markets. Within Luxembourg, the community of business and legal experts strengthened their established practices of regulatory engineering and their relationships with the political sphere. The use of overlapping roles, familial ties, and the dynamic interpretation of laws enabled Luxembourg to nurture the parallel growth of its internationally oriented mutual fund and Eurobonds markets. In so doing, the Grand Duchy deepened its overarching strategy of bifurcation of sovereignty, leveraging its status as a small state to create advantageous conditions for tax avoidance.

Business-Government Nexus in the Strengthening of Luxembourg's "Power of the Powerless" within Europe, 1970s–1980s

Up to the late 1980s, Luxembourg further strengthened its local mutual fund industry. It cemented its role as a global tax avoidance hub by strategically maneuvering the process for regulatory harmonization of the mutual fund market at the European level.

As early as 1968–1969, Pierre Werner had opposed a European Commission's proposal for a unified withholding tax on holding companies' revenues. In 1968, Werner appointed Bernard Delvaux, champion of the most liberal dynamic interpretation of the Holding Act, to represent the country in these negotiations.[108] While Werner lobbied against the harmonization, the European Commission eventually dismissed its initial harmonization plan owing to a phase of turbulence in the financial markets in 1968.[109] Yet, starting in 1973, the Council (managing the Commission's directive proposal) began discussions around a new draft directive aimed at harmonizing European Undertakings for Collective Investment in Transferable Securities (UCITS), namely the mutual funds that the directive allowed to be marketed and sold across EU member states.[110] A crucial trigger was likely the burst of a major scandal involving IOS, particularly its leading fund in Luxembourg, the IIT, plagued by mismanagement and structural recourse to Ponzi schemes.[111]

[107] Werner, *Itinéraires luxembourgeois*, II, 98.
[108] Werner, *Itinéraires luxembourgeois*, II, 94.
[109] Werner, *Itinéraires luxembourgeois*, II, 94.
[110] *Fonds Communs de Placement, Statistiques, Historique des fonds d'investissement au Luxembourg, Le marché des fonds en Europe*, box I-813, Archives de la Banque Nationale de Belgique (ABNB).
[111] Majerus, "This Is Not a Scandal."

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The debates on the harmonization of the UCITS market began in the second half of the 1970s under the Council's 6-month rotating presidency, led by Luxembourg's new Prime Minister Gaston Thorn. Although Thorn had won Luxembourg's general elections in 1974 against Werner's CSV, his government never openly challenged the country's holding system. Moreover, Werner, Thorn, and Jacques Santer began their careers as lawyers in the same law firm, Tony Biever's, a sort of "nursery of statesmen" in the Grand Duchy.[112] This aligns with the corporatist approach of small states, where political elites often belong to tight-knit, culturally homogeneous networks, transcending party orientation.[113] In this regard, Gaston Thorn, who was also going to serve as the head of the European Commission between 1981 and 1985, evocatively spoke of Luxembourg being "run by a football team" as a way to describe the capability of Luxembourg's entrepreneurial and political elites to shape the country's social and business environment (especially in terms of financial and corporate regulation) through the concerted work of a highly interconnected community of professionals.[114]

Meanwhile, the CCB (which in the 1980s changed its name to IML Institut Monétaire Luxembourgeois, and then in Financial Sector Supervisory Commission (CSSF) in 1999) directly participated in the debate on drafting the UCITS directive with its emissaries either in the Luxembourgish delegation at the Council, or in the inter-members committees of advisors for the Council.[115] The Luxembourg regulator sent Charles Kieffer, a director of IML specialized in the financial securities market, who would then become the head director of the "Investment Activities (other professionals of the financial sector, stock exchange activities, securities markets)" department of the CSSF in 1999, to represent Luxembourg in the "Committee of Permanent Representants."[116] Kieffer's task was to advise the Council on the objections raised by national delegations and the state of the works on the proposals for the Council's UCITS directive.[117]

The UCITS directive aimed to protect small investors, standardize the market, and allow free movement of fund shares in the European Community.[118] In the process of assimilation, Luxembourg's legislators and their delegates at the Council were nevertheless going to advocate for preserving Luxembourg-domiciled UCITS's low rate of capital stock taxation and zero withholding tax on distributed dividends.

[112] Jacques Santer, Interview with authors, 1 Oct. 2021; Jean de La Guérivière, "La montée vers Bruxelles de Jacques Santer," *Le Monde*, 18 May 1995.

[113] Dörry, "The Role of Élites"; Hampton and Christensen, "Treasure Island Revisited."

[114] Kremer, Interview, 11 Jan. 2023.

[115] Chèvremont, Interview, 23 Nov. 2022.

[116] *CIRCULAR CSSF 99/1 on the establishment of the Commission de Surveillance du Secteur Financier*, 12 Jan. 1999, 2, CSSF. See also: "Le parcours de Jean-Nicolas Schaus," *Paperjam*, accessed 6 Jan. 2025, https://paperjam.lu/article/news-le-parcours-de-jean-nicolas-schaus.

[117] *Rapport du Groupe des questions économiques (Établissement et Services) au Comité des représentants permanents sur la proposition de directive du Conseil portant coordination des dispositions législatives, réglementaires et administratives concernant les organismes de placement collectif en valeurs mobilières, Problèmes sur lesquels le Comité est appelé à se prononcer*, 22 Oct. 1985, Council of the European Union Archives (CEUA), 9738/85.

[118] *Proposition de directive du Conseil portant coordination des dispositions législatives, réglementaires et administratives concernant les organismes de placement collectif en valeurs mobilières, Exposé des motifs*, 1, 10, R-1095/76, CEUA.

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Moreover, as pointed out by coeval analyses of the local fund market dynamics of the time, Luxembourg could leverage the absence of withholding tax with strict rules on the confidentiality of fund investors' banking information under domestic law, which eventually was complemented by a dedicated law on banking secrecy.[119] As a result, the Grand Duchy's delegation strategically delayed the approval of the UCITS European directive. In Council discussions, they consistently opposed any attempts to introduce fiscal harmonization features within the UCITS directive framework, mainly advising against issuing a parallel directive dedicated to this purpose, which would have "postponed sine die" the "simultaneous adoption" of the two directives.[120] This approach continued until an unexpected alignment of interests emerged with France and Germany. Unlike Luxembourg's fund market, which focused entirely on international investors at the time (Figure 2), France and Germany's markets comprised primarily domestic investors.[121]

France, in particular, was the second-largest hub for mutual funds capital stock after the USA, based mainly on investments from its national investors, until Luxembourg surpassed it in 2004.[122] During the Council debates between the late 1970s and 1985, when the UCITS directive was finally issued, the Greek, Belgian, and Irish delegations repeatedly expressed concern about extending fund shares' free movement without a parallel fiscal harmonization process. Greek delegates, in particular, warned of capital outflows and increased risks of tax evasion owing to attractive tax advantages in certain fund markets, such as Luxembourg.[123] In contrast, Germany, and France sought to maintain their existing fiscal frameworks, supporting their well-established, domestic market-oriented fund industries, and strongly

[119] Alex Schmitt, *Investment Funds in Luxembourg*, 54, Fonds Communs de Placement, Statistiques, 1993, box I-813, ABNB; André Elvinger, *Investment Funds – Regulations – Taxation – Evolution*, proceedings of Seminar, Nov. 1988, Institut Universitaire International Luxembourg, Association des Juristes de Banque, Fonds Communs de Placement, Statistiques, box I-813, ABNB. Unlike Switzerland, Luxembourg did not establish a formal banking secrecy framework until 23 April 1981, when a unanimous vote in the Grand Duchy's Chamber passed the "banking secrecy" law. This law, along with its updated version on 5 April 1993, made breaches of confidentiality by banking operators, institutions, or professionals a criminal offense under Luxembourgish law. Although Luxembourg-domiciled UCITS and their management companies were not directly subject to these banking secrecy laws, the framework still applied to banks acting as distributors of investment fund shares or registering agents for funds.

[120] *Proposition de directive du Conseil portant application, aux organismes de placement collectif, de la directive du Conseil du . . . concernant l'harmonisation des systèmes d'impôt sur les sociétés et des régimes de retenue à la source sur les dividendes (présentée par la Commission au Conseil)*, 18 July 1978, CEUE_SEGE-COM (1978)0340, European University Institute Historical Archives (EUIHA); *Rapport du Groupe des questions économiques (Établissement et Services) au Comité des représentants permanents sur la proposition de directive du Conseil portant coordination des dispositions législatives, réglementaires et administratives concernant les organismes de placement collectif en valeurs mobilières, Problèmes sur lesquels le Comité est appelé à se prononcer*, 22 Oct. 1985, 3, 9738/85, CEUA.

[121] *Historique des fonds d'investissement au Luxembourg, Le marché des fonds en Europe*, Fonds Communs de Placement, Statistiques, box I-813, ABNB.

[122] Investment Company Institute, *Investment Company Factbook: A Review of Trends and Activities in the Investment Company Industry* (2004). Accessed 6 Jan. 2025, www.icifactbook.org.

[123] *Addendum au Rapport du Groupe des questions économiques (Établissement et Services) au Comité des représentants permanents sur la proposition de directive du Conseil portant coordination des dispositions législatives, réglementaires et administratives concernant les organismes de placement collectif en valeurs mobilières, Annexe, Communication de la délégation hellénique*, 21 May 1984, 3, 7120/84, CEUA.

Figure 2. Sales of Luxembourg-domiciled investment fund shares (LUF million) to Luxembourg-resident and non-resident investors, 1968–1977. (Source: Informations sur les ventes et rachats de parts de fonds d'investissement au Grand-Duché de Luxembourg [Information on the sales and redemptions of investment fund shares in the Grand Duchy of Luxembourg, managed by Luxembourg-based financial intermediaries], box 9813, CSSF. Authors' calculations.)

opposing fiscal harmonization projects. Ultimately, the interests of the largest and most influential states prevailed, and UCITS were marketed in Europe without harmonized capital stock and withholding taxation. This gave Luxembourg a significant advantage, allowing it to promote favorable fiscal conditions more efficiently throughout the European Community. As a result, Luxembourg solidified its position as a leading global mutual fund hub by the early 1990s.

Meanwhile, Luxembourg industry representatives acted swiftly at the national level. They strategically accelerated the transposition of the draft directive into the Luxembourgish regulatory framework, aiming to secure a "first mover advantage" in the European market.[124] In parallel with the ongoing debate on the draft of the UCITS directive at the Council, the IML organized bi-weekly concertation tables (the so-called "Comités des Valeurs Mobilières" or "Comités"), where the main actors operating in Luxembourg's fund market could contribute to the drafts on the transposition of the European directive which eventually resulted in two national laws in 1983 and 1988.[125]

One of the first outcomes of the Comités was the introduction of some of the main principles of the UCITS directive in Luxembourg in August 1983, 2 years earlier than

[124] Dörry, "The role of élites"; Dörry, "Strategic Nodes in Investment Fund Global Production Networks: The Example of the Financial Centre Luxembourg"; Dariusz Wójcik, Michael Urban, and Sabine Dörry, "Luxembourg and Ireland in global financial networks: Analysing the changing structure of European investment funds," *Transactions – Institute of British Geographers (1965)* 47, no. 2 (2022): 514–528.

[125] FINLUX Database; Chèvremont, interview, 23 Nov. 2022; Kremer, interview, 11 Jan. 2023; *Loi du 25 août 1983 relative aux organismes de placement collectif, Mémorial A*, Legilux; *Loi du 30 mars 1988 relative aux organismes de placement collectif, Mémorial A*, Legilux.

the promulgation of the final UCITS directive in 1985. Unsurprisingly, the leading Luxembourgish law firms involved in the mutual fund market had their senior partners regularly attending these meetings. For example, André Elvinger, founder of Elvinger and Hoss, the most successful local law firm in investment funds' intermediation since the 1960s. Or Jacques Delvaux, son of Bernard Delvaux, who the IML had also appointed as the leading liquidator of IOS's IIT.[126] The primary banking intermediaries based in Luxembourg (including the banks BIL, KBL, and BGL), managing high volumes of capital transfers through sales and redemptions of shares of mutual funds, also sent high-ranking representatives.[127] Furthermore, the IML invited two additional private firms: the Compagnie Fiduciaire (the future Deloitte), which was represented by its Luxembourgish founding member Jean Hamilius (who had also been MP, Minister for Agriculture, and for Public Works in Thorn's government of 1974–1979) and French economist Jeanne Chèvremont, representing the Brussels-based agency of Coopers & Lybrand (the future PWC).[128]

Chevrèmont's involvement was both innovative and decisive in two key respects. Not only was she the sole woman in an all-male environment, but arguably the first foreign national to have directly participated in the transposition and drafting of legislation regulating the fund market in Luxembourg:

> "I wrote myself an article of the [1988] law [. . .], and so I made the proposition which was discussed, and so it was really a working together in fact."[129]

Additionally, Chèvremont contributed to quickly translating Luxembourg's fund law of 1988 into English. This served as a marketing tool for Coopers & Lybrand and facilitated further internationalization of Luxembourg's fund market. She explained:

> We had [the law] immediately in English, and we knew that this law was of interest for the Anglo-Saxon fund managers, particularly the US fund managers, who were looking for a gateway to Europe for some of their products. [. . .] And so, with our law ready in English, one week later [after its promulgation], of course we had a marketing tool. Next, I started to travel around [the world] and [. . .] organized a lot of meetings with the clients.

Finally, attending the Comités, there was also the Luxembourgish economist Yves Mersch.[130] After working at the Ministry of Finance led by Jacques Santer in the early 1980s, Mersch became an advisor of the IML (between 1983 and 1999), and was

[126] *Liquidation du fonds IIT*, box 16656, CSSF; Chèvremont, interview, 23 Nov. 2022. For example, in 1984 the representant for KBL in 1984 was Damien Wigny, administrateur-directeur of Luxembourg KBL.

[127] *Comité OPC Documents de Travail I, 1984–1987*, letter of Damien Wigny to Edmond Jungers, secretary of the Comité "Valeurs Mobilières," IML, 7 Dec. 1984, box C000016745, CSSF; *Informations sur les ventes et rachats de parts de fonds d'investissement au Grand-Duché de Luxembourg*, box 9813, CSSF; Chèvremont, interview, 23 Nov. 2022; Kremer, interview, 11 Jan. 2023.

[128] "History," *Deloitte Luxembourg*, accessed 6 Jan. 2025, https://www2.deloitte.com/lu/en/pages/about-deloitte/articles/history.html"; Thewes, *Les Gouvernements*, Service information et presse du gouvernement Luxembourgeois, Département edition, 183; Chèvremont, Interview, 23 Nov. 2022.

[129] Chèvremont, Interview, 23 Nov. 2022.

[130] Chèvremont, Interview, 23 Nov. 2022.

appointed by Santer as Government Commissioner at the LuxSE (between 1985 and 1989), which he was representing at the Comités meetings.[131]

Once again, the clannishness and tight relationships between the state and finance permeated Luxembourg's regulatory process. On the one hand, as Chèvremont observed: "there were lawyers that had political responsibilities and probably this affected how the laws came through." On the other, there "might have been lobbying at the government level" through the LuxSE representatives.[132] Indeed, according to Jacques Santer, "his team" at the Ministry of Finance was occupied with parallel drafting work on the fund laws of 1983 and 1988, integrating discussions from the Comités. Mersch could have served as the link to this second group, which included government financial advisors, and Edmond Israel, the former head of LuxSE and a key figure in the rapid development of the Euromarkets in Luxembourg.[133] Santer later described Israel as an influential financial policy advisor, and "a good family friend."[134]

In sum, between the late 1960s and 1980s, Luxembourg policymakers and representatives in European institutions integrated usual practices of overlapping roles and dynamic legal interpretation at the national and international levels with "strategic planning for the assimilation of European directives." In some cases, they delayed approval, while in others, they expedited the transposition process, depending on what was most beneficial for Luxembourg's mutual fund industry. This combined approach strengthened Luxembourg's implementation of its long-term strategy centered on sovereignty bifurcation through its legal framework for holding companies and mutual funds. This illustrates Luxembourg's tendency to leverage its small size within European institutions to further its status as a tax avoidance hub, exemplifying the concept of "the power of the powerless," where weaker state actors can use their limitations, such as their small size, to gain an edge in the international arena.

Conclusions

This article reviewed the emergence and internationalization of the Luxembourg mutual fund industry between the 1940s and the 1980s by analyzing diverse archival and oral history sources. We argue that Luxembourg's dense community of policymakers, legal professionals, and financiers played a pivotal role in the country's post-war specialization in financial services by consistently applying bifurcation of sovereignty strategies to the regulation and organization of its mutual fund industry. This process involved progressively expanding areas with lenient or zero taxation, specifically designed to attract international investors. The analysis of our historical evidence suggests that being a small state facilitated this development.

Notaries, business lawyers, and professionals of the fund sector operated as "code masters" at the intersection of politics and business, wearing multiple hats, and using their deep knowledge of fiscal regulation and European legal mechanisms to advance

131 Yves Mersch, *Financial Governance in the EU* (European Court of Auditors), accessed 6 Jan. 2025, https://www.eca.europa.eu/sites/FinancialGovernanceEU/Documents/Yves-Mersch.pdf.

132 Chèvremont, Interview, 23 Nov. 2022.

133 Dörry, "The Role of Élites."

134 Santer, Interview, 1 Oct. 2021.

the local financial industry. The analysis highlights how Luxembourg officials acknowledged and actively developed systematic practices of regulatory engineering (in the form of strategies such as dynamic interpretation of laws and strategic planning of directive approval), and widespread acceptance of conflicts of interest (in the form of overlapping roles and revolving door practices) between finance and politics.

The analysis illustrates how Luxembourg advanced its specialization by combining social corporatism, marked by cooperation and informal government administration typical of small states, with the knowledge-sharing and informal connections characterizing communities of practice in highly specialized service industries, such as finance. Our diverse source base was crucial in demonstrating the role of such network dynamics. For instance, confidential documents from Banque Lambert revealed that Luxembourgish business lawyer Bernard Delvaux played a critical role in the emerging mutual fund industry, acting as the bank's legal representative and as an influential figure in Luxembourg's regulatory institutions. Luxembourg's regulators endorsed Delvaux's juridical publications on a dynamic interpretation of H29, eventually giving them legal authority. Oral histories and archival evidence from the Comité des Valeurs Mobilières, responsible for drafting Luxembourg's mutual fund laws in the 1980s, further confirm the significant influence of private institutions (legal firms, audit companies, and banks) in shaping national financial regulations. Since the interwar period, the close intertwining of Luxembourg's private and public spheres played a crucial role in the country's early development as a financial hub. This relationship was instrumental in its specialization in mutual funds and other financial instruments, such as Eurobonds, helping transform Luxembourg into a global financial cluster after World War II.

Overall, these findings provide two novel contributions. First, they enhance the understanding of the mechanisms leading to the clustering of financial services, showing that the business-government cooperation in regulatory sophistication, typical of small states' dense communities, can support the emergence and growth of financial specialization. Second, this research contributes to the sparse scholarship on the European mutual fund industry and its global expansion concerning tax avoidance practices in small and microstates, which remains a relatively underexplored topic.

The reconstruction of Luxembourg's specialization, in turn, highlights some central aspects of the broader scholarly discussion on small states. On the one hand, the deep, multigenerational relationships within the country's elite, and "managed intimacy" strengthened cohesion within Luxembourg's governance and solidified the close ties between government and finance. On the other, Luxembourg's case is particularly relevant because the country was able to facilitate specialization, which is generally a challenge in small states owing to multifunctionality, and through foreign experts' involvement in their legislative process. Furthermore, like other small states specializing in offshoring, such as Curaçao, Luxembourg's mutual fund industry demonstrates how influential financial elites from neighboring nations often utilize smaller countries to push through regulations difficult to implement at home. In its early stages, Luxembourg's mutual fund specialization was closely linked to Belgian firms and financiers, reflecting a deep entanglement between them.

Luxembourg's elite skillfully leveraged its status as an EU founding member and its small size to carve out a niche in tax optimization. While this strategy fuelled the

Grand Duchy's economic growth, it also created an environment ripe for preferential treatment, conflicts of interest, and revolving doors between the public and private sectors. This arrangement, which served the interests of both local and European parties, surpassed mere "opportunistic pragmatism." It frequently involved compromising ethical standards at both national and EU levels, thereby contributing to a global capitalist system that relies also on tax evasion.

Further historical investigation into the factors, including the interaction between business and political elites, that drove the development of successful fund markets in other small states, such as Ireland, since the 1990s is needed. Comparative business history analyses are essential to understand the conditions that provide a sustained comparative advantage, or enable successful coexistence for one small state over another specializing in the same financial instrument.

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